

MR. MASTEL: Thank you, Mr. Chairman. I am indeed happy to be here today.

Earlier this week our telex sent a written testimony to the Committee. Instead of reading that today, I am just going to summarize briefly some key provisions of my comments.

As you saw already today, it is impossible to talk about trade with China without talking about some lofty topics, like security reform in China, et cetera.

But it seems to me that when it comes down to the details of a trade arrangement with China, it comes down to how we evaluate the quality of the trade agreement we struck and is that agreement enforceable, a very mundane issue, but it seems to me that all of the other benefits will not flow unless the agreement is enforceable.

For that reason, I focus my comments on China's record of trade enforcement and some ideas about how we might improve that record in the future.

First of all, there has been a lot of commentary, general commentary, about the quality of China's trade agreement compliance record in the past.

Most of the people who make these comments tend to group a whole bunch of agreements on issues like

nuclear nonproliferation, shipping lanes together, and say, "Well, kind of overall, it doesn't do too bad."

Unfortunately, that's more than comparing apples to oranges. Trade agreements are a very different kind of agreement. There are very different kinds of incentives for cheating. I think if you want to know about China's record, you have to compare trade agreements with trade agreements.

In the last ten years, the U.S. has struck four trade agreements, government-to-government agreements, with China on trade matters. In 1992, on intellectual property, in --

COMMISSIONER LEWIS: Excuse me. Could you speak a little more slowly?

MR. MASTEL: I'm sorry. Yes.

COMMISSIONER LEWIS: I can't quite digest.

MR. MASTEL: That's the problem with speaking without written remarks, I guess.

There are four important agreements the U.S. has struck with China in the last ten years that I think are relevant to this discussion. The first one is the 1992 agreement on intellectual property enforcement. The second is a 1992 agreement on market access. The third is actually a series of agreements

on textile shipments from China. And the fourth is an agreement on prison labor. Now let me evaluate each of the agreements separately and talk about China's record with compliance and enforcement problems, if I could.

Again, the details of each of these are written in my testimony. And there are a lot of statistics you might want to look there to get a reference on. Let me just make some general comments.

First, intellectual property agreement in '92. This is probably the best-known U.S.-China agreement on trade. It was struck in 1992 after about a decade of hemming and hawing about no intellectual property protection in China, which pretty much everyone agrees was not very good at that point.

So in '92, an agreement was struck that put China's intellectual property laws, patent, copyright, trademark laws up to pretty much a global standard. The laws really were very, very good. Unfortunately, on the ground, almost nothing changed in China. Piracy became an epidemic problem.

Now, in 1995, the Clinton Administration recognized the problem and raised the issue with China and threatened sanctions if China did not improve its record. And China made some more promises.

Unfortunately, only about a year later, 1996, those promises were not fulfilled. Piracy had actually risen, had become a larger problem. China was now, in fact, exporting some of the pirated intellectual property goods out of China to the rest of the world.

They were showing up as far away as Canada, Eastern Europe. And so once again, the Clinton Administration confronted China about intellectual property piracy and threatened sanctions.

In the end, China agreed to improve its enforcement, and it listed some steps it would take to improve intellectual property enforcement. And so in 1996, the Clinton Administration declared victory. And there was some reason to think that progress had been made.

If you look at the agreement overall, however, you can argue that enforcement is better now than it was in 1995 or 1992. But it's almost impossible to say it is good.

In fact, if you look at the overall economic impact of piracy in China, according to the industry estimates, the cost is now higher than it was

in 1995, when the effort began. The total cost of piracy in China is now higher than it was in 1995.

That's an important statistic. Whenever you're thinking about China's record here, I think it's important to look back at that.

There may be some improvement. We have seen more ever serrate factors. We have seen more steamrollers crushing pirated CDs and so forth in China. But the real impact has been pretty small. And, more importantly, -- I think this is the key point I put in my testimony -- the issue here is not just some guys on the street pirating CDs and so forth.

The Chinese government is directly involved in many aspects of intellectual property piracy. The PLA has made it a major cash cow for their operations. This is not some kind of back alley operation. It's an issue in which the Chinese government is directly involved in violating an agreement with the United States.

And, again, it may be true that after a full court press several times, the US had actually improved the quality of intellectual property protection in China, but it has improved it very marginally.

We start from a level of almost zero. And we may have increased it to five percent, but we still have a huge problem in China. This is after a decade of trying, a decade of full court effort backed up by the Administration and backed up by the industry. We have not gotten that far, even on the case where we made the best effort. On other cases, we have not really made so much of an effort.

The market access agreement in '92 was another example. I think it was mentioned earlier in the panel. This was really a sweeping agreement that covered a whole range of Chinese trade barriers, made a lot of commitments on trying to lower non-tariff and tariff barriers, and the Administration says that China has generally implemented the agreement, used the term "generally."

I think that's probably generally correct. There are a lot of things China has done. Some of the easily verifiable steps have been taken by the Chinese, but there are still enormous enforcement and compliance problems in China. Let me just list three, again for lack of time.

First of all, in 1992, China agreed to end the import substitution policies, policies that

substituted imports with domestic production. But in two subsequent state plans, on pharmaceuticals and on automobiles, they still use the term "import substitution." Again, you still see import substitution in a lot of the lower-level plans on things like electric generating, generating equipment, and so forth.

Secondly, China agreed to eliminate a class of trade barriers called import licenses in 1992. It eliminated the import licenses but then shortly thereafter put in place import registration requirements, which were pretty much the same thing.

You have seen a lot of cases where China had raised new barriers, renamed barriers after 1992. So the overall net impact has been limited.

Third, China also agreed to make public all regulation on trade and investment in 1992. In many cases, it's done this, but still in the government procurement area, a very important area in China, the regulations are still not made public.

So there are still some very significant areas where China has not met the letter of the agreement it struck with the United States. And these are not small issues. They have been raised again and

again with China's officials. There's been no even official denial of these problems. So, again, compliance has been a serious problem with market access.

Well, for lack of time, let me summarize the last two issues. On the textile agreement, this is the agreement that the U.S. has with China regulating the shipments of textile under the multi-fibre agreement.

Now, the U.S. Customs Service over the years has estimated that they had a problem with illegal transshipment. Goods made in China but illegally labeled coming from Hong Kong or from Macao is enormous. They have estimated that at different times two billion dollars in transshipment and ten billion dollars in transshipment.

I'm not exactly sure what it is, but clearly there are enormous problems in transshipment that actually are large enough to inflate the trade deficit with China if we knew what the actual volume was.

The last agreement with China is one on prison labor. Now, the State Department in its most recent report essentially said that this agreement has



been a failure because China has failed to comply with it and China has unilaterally redefined terms to make the agreement meaningless.

There may be more discussion about this later, but, again, I quoted the State Department directly in my testimony. I think they've said more than I could ever say to explain how poorly this agreement has performed.

Let me conclude by making three points. First, the problem with China is a unique problem. Many people, including some on this panel, would argue that other countries have violated trade agreements. And that's certainly true. We have problems with Japan, with Europe, with Korea.

But I think you would have difficulty finding any single country with which you had a problem with every single agreement we have negotiated on this magnitude.

This is a unique problem. And it certainly is something that we should consider, including other trade agreements with China or setting up U.S. trade policy toward China.

We should be very careful to recognize the problems we had in the past and set up new procedures

to deal with them. And we shouldn't be blind to what we have learned from the past.

Secondly, this problem is deeper than just simply cheating. As I said, many countries have cheated on trade agreements with the United States over the years. It's usually a matter of their pleading some domestic constituency that would be hurt by the trade concession.

It's a very common problem. But in China, I think it goes beyond that. You have all of the normal constituencies arguing against liberalization, but you have an additional problem that China lacks a rule of law.

The central government does not have rule of law authority over the economy. As a result, the central government of China really can't obligate China's complex mix of state-owned enterprises, government ministries, the PLA, et cetera, to go along with a trade agreement that it strikes.

As we have seen in areas like intellectual property piracy, like market access, Chinese government ministries have been directly involved in the violations. This is not a back alley problem. It's a problem of the government not doing what it says it

would do. And that's why it's a very serious issue with China.

The last point I would make is that enforcement should be critical in deciding about all trade agreements. We have now before us or the Congress has before it the issue of permanent NTR for China. Central to that question is: Do we want China to be a WTO member?

Again, many lofty issues come up in connection with that. But it all comes down to can this trade agreement be enforced? If it will be enforced, there will be real economic benefits.

There will be secondary benefit in terms of encouraging the rate of reform in China. It will increase the power or the form of it in China to change things, make China a more liberal economy. But if it cannot be enforced, none of those benefits will materialize.

So the issue of enforcement is not just some mundane side issue. It's very important. If we want to see real benefits from a trade agreement with China, we have to be sure of enforcement. And so far we have not had a very good record of taking the

measures necessary to make sure that agreements are enforced.

VICE CHAIRMAN PAPADIMITRIOU: Thank you, Mr. Mastel.

Mr. Wu?